Fiscal Update: September 1996

Trends in the Labor Market

June's unemployment rate of 4.5% marked an all-time-low in the state of Michigan. This was short-lived, however, as July's unemployment rate jumped 0.3 percentage points to 4.8%. This is still well below the U.S. rate but represents a narrowing of the gap. The increase can be attributed primarily to vacation shutdowns in the manufacturing sector, and thus may be a temporary phenomenon. The U.S. unemployment rate decreased to 5.3% in June, but rose by 0.1 percentage points in July.

- 1996 year-to-date average unadjusted wage and salary employment in Michigan is 35,000 jobs over the average employment level of 1995.

- With the exceptions of March and July, average employment for the year has remained steady in the manufacturing sector and has increased in the service sector. Some of this increase can be attributed to the business services industry, indicating an increase in the use of temporary employees and out-sourcing.

The National Economy

Composite Indices

In predicting the future path of the economy, economists traditionally look at three types of indices: the composite index of leading economic indicators, the composite index of coincident economic indicators, and the composite index of lagging economic indicators. The value of each index is derived from several economic indicators and is now calculated by The Conference Board, Inc., New York, N.Y.

- The composite index of leading economic indicators rose for the sixth consecutive month. It reached 103.1 in July, an all time high. This is 0.2 percentage points above last month, and represents a 2.0 percent increase since the beginning of the year. For the first half of the year, 9 of the eleven component indicators increased, including all five of the components related to manufacturing. Only two, building permits and consumer expectations, declined. Unfilled orders for durable goods increased 2.1 percent in 1996 following a rise of 1.8 percent in the last half of 1995. This bodes well for the state's auto industry, and suggests continued economic growth through the end of the year and into 1997.

- The composite index of coincident economic indicators has been climbing steadily for the past five months. It increased by 0.5 percentage points in June, reaching 121.1. This substantiates the view that the economy is in the midst of a steady growth phase.

- The composite index of lagging economic indicators, after downturns at the beginning of the year, increased in May by 0.4 percentage points, but declined slightly by 0.1 percentage points in June. This confirms the solid but unspectacular growth experienced in the first quarter of 1996.

Components of Gross Domestic Product

Gross domestic product (GDP) measures the total value of all final goods, services, and structures produced in the United States. GDP growth is the standard measure of the performance of the economy, and has four main components --personal consumption expenditures, gross private domestic investment, government purchases of goods and services, and net exports (exports less imports) of goods and services. GDP increased by a robust 4.8% in the second quarter of 1996. Strong growth in investment and government expenditures fueled the increase, whereas growth in consumption and net exports were relatively stable from the first to the second quarter.

- Growth in investment expenditures rose 11.1% in the second quarter. Although growth in fixed investment decreased, increases in residential and business inventory investment more than made up the difference.

- Government expenditures increased by 8.2% in the second quarter, 10.7% at the federal level. State and local spending rose by 6.8%, largely due to recoveries from the harsh winter.

- Net exports (exports minus imports) decreased from -$104.0 billion in the first quarter of 1996 to -$115.2 billion in the second quarter.

- Consumption climbed by a robust 3.4% percent (preliminary) in the second quarter of 1996, slightly behind the 3.5% pace of last quarter, and can be attributed primarily to an increase in durable goods expenditures. This is expected to slow in the future considering the extent to which consumers are in debt.

Inflation and Capacity Utilization

Inflation is measured as the percent change in the average price level of the economy over time. The capacity utilization rate is measured as the amount of output produced in an industry as a percent of that industry's maximum capacity. The capacity utilization rate is thought to be a good indicator of impending inflation.

- When the economy is growing quickly, businesses are producing at a high rate and using as much of their productive capacity as possible. As maximum capacity is approached, upward pressure on prices is exerted because businesses are not able to produce beyond a certain amount. In response, they raise prices. When this occurs in a sufficient number of industries, the result is inflation.

- The capacity utilization rate of the durable goods sector is often related to the state's inflation rate. From the chart, one can see movements in inflation follow movements in the capacity utilization rate.

The Michigan Page

Personal Income and the Auto Industry

Growth in state tax revenue is largely determined by growth in state personal income. Of the 50 states, only Michigan had a net decrease in personal income growth in the first quarter of 1996. This is attributed primarily to the GM break plant strike near the end of the quarter. Prior to this, Michigan's personal income growth ranked among the highest in the nation.

- The U.S. Department of Commerce reported that Michigan's personal income totaled $226.7 billion in the first quarter of 1996, a decrease of 0.6% (the U.S. increased 1.6%), and well below the 1.4% increase of the previous quarter.

- Real disposable income is an indicator of future expenditures in the durable goods sector. This sector, comprised of light vehicles and other goods, is an important contributor to the Michigan economy. Real disposable income for the U.S. increased by 0.7% in the second quarter of 1996, falling from a revised 1.2% increase in the first quarter. This marks the second quarter in a row that growth in disposable personal income has declined and is well below the pace of the last half of 1995 when the average growth rate was 3.4%. This may indicate, contrary to other data, an imminent tightening of consumer spending on durable goods.

- Year-to-date 1996 U.S. car and light truck sales totaled over 9.1 million units, up 4.4% over 1995 levels. Light trucks were once again the primary engines of growth, posting a 7.7% gain over 1995 levels; cars were up 2.0%. Both car and light truck sales dipped slightly in July. The proportion of imports to domestic auto sales has increased in the light truck market but decreased in the car market. 1996 year-to-date U.S. production is 4.4% below 1995 levels as plants are still making up for the GM brake plant strike in March. July production was 34.7% ahead of July 1995 levels.

For a copy of this report (with accompanying tables, graphics, and footnotes) prepared by Stephen Marasco under the direction of the HFA economist, please contact Mitch Bean or call the HFA office at 517.373.8080.

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